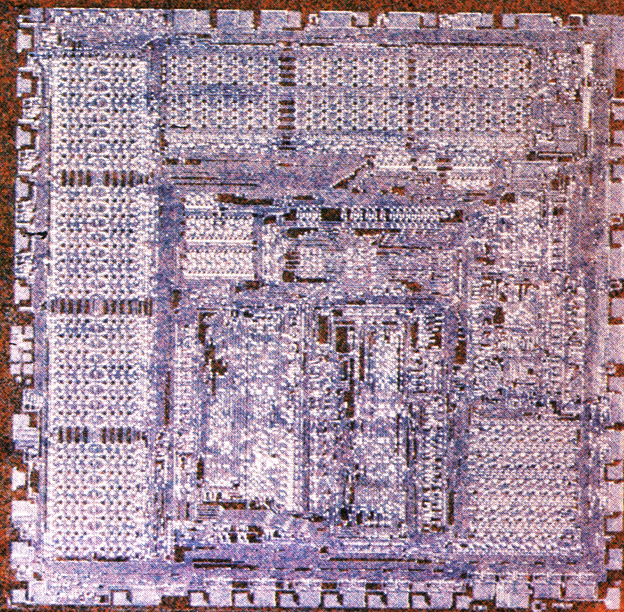


"from a dream to reality"



Annual Report
1976



"From a dream to reality"

The cover of Commodore's 1976 Annual Report was created originally as a poster by Alain Zimeray in Paris. Mr. Zimeray is the son of Georges Zimeray, president of Sonotec, Commodore's largest wholesaler in France.

To the Shareholders

In 1975 your Company pledged strong management and financial controls, which would then be combined with careful marketing strategy to produce improved profitability and liquidity.

We were successful in 1976. Let's look at the bottom line:

- Gross profit increased by 135%.
- Operating expenses were reduced by over a million dollars.
- Interest expenses were cut by 40% through a reduction in short term debt of two million dollars.
- Current trade liabilities were reduced by four and a half million dollars.
- Your ownership equity increased by almost three million dollars.
- Earnings set a new record at \$2,911,197 or \$2.26 per share.

OUR STRATEGY PAID OFF

We made it our business to increase market share wherever this would prove profitable. In Europe we achieved the largest share of market of any calculator manufacturer; Europe accounted for just under 75% of your Company's calculator sales as contrasted with 60% in 1975 and 25% in the year prior. In North America, where industry profitability has been under the hammer for two years, we decreased our emphasis . . . and our expenses.

We were able to reduce selling expenses and general and administrative expenses each by a half million dollars. But we left research and development expenses virtually intact, in recognition of its importance.

Fiscal 1976 saw Commodore's leadership in scientific calculators, our most profitable category, increase dramatically. The SR4190, to date the most powerful preprogrammed scientific calculator in the world, and developed through our own R & D, became an instant winner. We were able to offer probably the industry's most complete value- and feature-packed line of scientifics. More than 80% of the calculators, both scientific and non-scientific,

produced by your Company in fiscal 1976 contained a Commodore-designed large scale integrated, metal oxide semiconductor (LSI/MOS) chip. The proportionate increase in sales of scientific calculators and the reduced cost of chips played a significant role in our increased gross profits.

OUR VERTICAL GROWTH CONTINUES

A major expansion after the close of the fiscal year occurred in August with an agreement in principle to acquire MOS Technology based in Valley Forge, Pennsylvania, an important producer of LSI/MOS chips and microprocessors.

This acquisition follows by less than a year the integration of Optical Diodes, Inc., the producer of light-emitting diode (LED) displays, into Commodore's semiconductor production group.

With this newest acquisition we now become a fully vertical semiconductor company with a potential for growth today that some of today's giants enjoyed a decade ago. We're now prepared, better than we ever have been before, to continue the Commodore pattern of being first in the market place with a better product for less money.

We have already launched our line of electronic watches. I fully expect that we will become a major force world-wide; we already are, in Europe, with our LED watches assembled in France.

WE EXPANDED WORLD-WIDE

1976 saw the opening of our San Remo, Italy sales agency. It also saw the opening of our new Hong Kong division which will be responsible for our production in the Far East. We plan to expand significantly the assembly of our own components — particularly of our LED displays, LSI chips and watch modules — in Hong Kong, the Philippines and Korea. Because Hong Kong is a free port, we expect to effect important savings in time and money with our shipping of components and completed goods.

We expanded our assembly facilities in England and the Orient and now in France. We have already installed in Palo Alto, in place of the calculator assembly facility (closed in June of 1976 to effect production savings), a major facility for the production of liquid crystal displays, in keeping with our commitment to liquid crystal watches.

OFFICE FURNITURE AND EDUCATIONAL SYSTEMS

In the year 1976, the steel furniture division in Canada increased its sales by 15% and accounted for 8% of Commodore sales. It continues to be profitable although profitability decreased in 1975 and 1976 due to increases in raw material costs. We have increased our share of the market in Canada significantly to where we are now number two in sales.

Commodore Educational Systems, on the other hand, presents quite a different picture. Sold only in Japan, these systems have consistently lost money. In fiscal 1976, Commodore Educational Systems Limited showed a net loss of more than one million dollars. Further retrenchment is planned in 1977 and your management is considering the closing of this operation completely.

YOUR COMPANY RESTRUCTURED

After the close of our fiscal year, the decision was approved at a general meeting of shareholders, to change your Company's corporate structure. Commodore Business Machines (Canada) Ltd. has now become Commodore International Ltd., a Bahamian Company. Each share of Commodore Business Machines will be exchanged for one share of Commodore International Ltd.

We have also streamlined the corporate structure to make our management even more effective. A comparison chart of our new structure, as contrasted with the previous, appears elsewhere in this report.

LOOKING AHEAD

As I look forward to the new fiscal year, I see a number of developments.

Calculators will continue this year to be the single most significant product of your Company. We see some stabilization in pricing and in the number of firms entering the market place. The increased importance of Commodore's position in scientific and financial calculators will continue in 1977. MOS Technology, ODI, and the Hong Kong division should reinforce Commodore's ability to produce better calculators for less money. We expect to maintain our position of leadership in Europe while reentering the North American markets.

In the third quarter (the first quarter of calendar 1977) we will be introducing the first series of dedicated preprogrammed scientific calculators and our first programmable calculator.

In spite of the fact that they will be extremely competitive in the market place, they should prove quite profitable.

Commodore's digital watches will become a major source of revenue in 1977. Watches should account for 30% of our sales. Liquid crystal watches will become a major force in the electronic watch market place. We have already made a major investment in liquid crystal production at our plant in Palo Alto. In spite of the fact that LCD watches are retailing today for appreciably more money than equivalent LED watches, in the fiscal year 1977 we will offer a liquid crystal watch to retail at \$19.95 . . . with profit to your Company.

We intend to enter the growing T.V. game market. The acquisition of MOS, with its game chip technology, will facilitate our entry.

We will also be actively engaged in microprocessors, a major advance in the semiconductor technology of LSI/MOS design. Microprocessor applications should represent a source for expansion of Commodore sales and profits in the years to come.

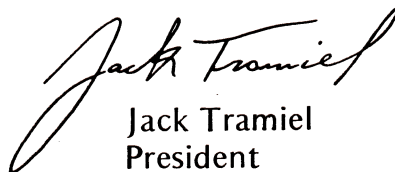
For the first time, your Company is prepared to offer components to original equipment manufacturers. These components would include the displays made by ODI and by our LCD facility and the chips and microprocessors — including all the Commodore-designed units — produced by MOS. We plan to set up a separate sales division. I foresee this becoming a significant part of our business.

I see further expansion of our office furniture business. I anticipate an improvement in profits for this division.

* * *

In reviewing 1976, I express, on behalf of your Board of Directors, my heart-felt gratitude to our suppliers, to our co-workers all over the world, and to our customers for making this our most profitable year.

1976 was successful. I pledge your Company's dedication in 1977 to maintaining the management controls that played so large a role in our profitability and liquidity in 1976.



Jack Tramiel
President
October 15, 1976

"We now become a fully vertical semiconductor company..."

"... The integration of Optical Diodes, Inc. ... this producer of light-emitting diode (LED) displays ... used in most of Commodore's calculators and all of Commodore's current line of watches."



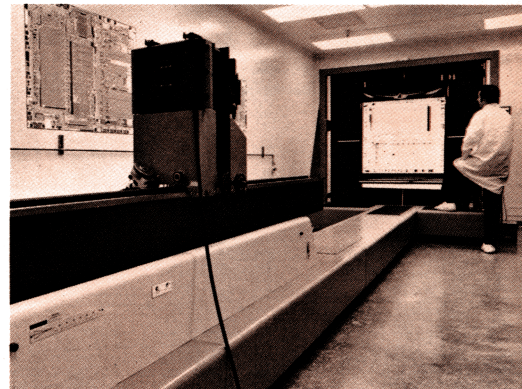
Inspecting wafers before scribing and assembling into light-emitting diode (LED) displays

"... A major facility for the production of liquid crystal displays, in keeping with our commitment to liquid crystal watches."



Filling glass sections with liquid crystals in one of last steps in creating liquid crystal display (LCD).

"... An agreement in principle to acquire MOS Technology ... an important producer of LSI/MOS chips and microprocessors."



Fabricating the mask from which chips will be produced.

"... Expanded our assembly facilities in the Orient, England, and now France."

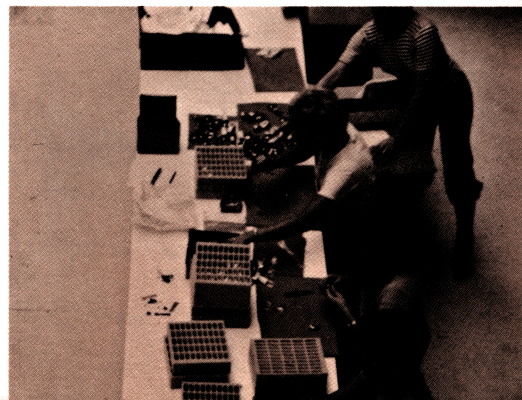
A calculator assembly line in Osaka, Japan.



... and in Eaglescliffe, England.



Assembling watches in Carros, France.



with a better product for less money.

...and other products

"We have already launched
our line of electronic watches . . ."



The complete watch is assembled in France. Commodore LED watches retail as low as \$20 (in the USA). Others in more deluxe styles retail for as much as \$40.

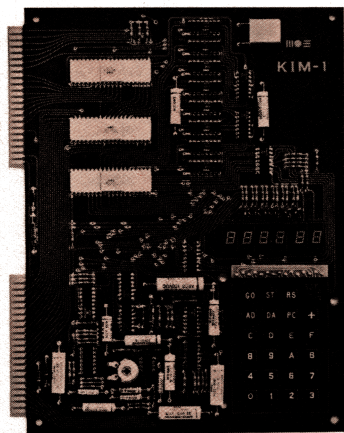
"The steel furniture division
increased its sales by 15% . . ."



The desks, bookcase and file shown are items in Commodore's very large selection of economy priced steel office furniture.

"Commodore Educational Systems . . ."

The system shown here includes an impressive array of audio-visual material designed primarily to teach the English language to Japanese customers.

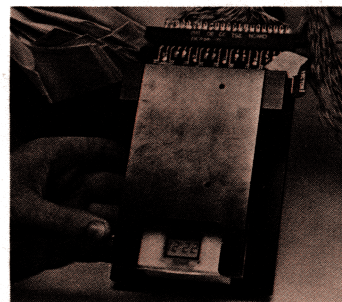


"We will also be actively engaged in microprocessors,
a major advance in semiconductor technology."

The Kim 1: For the first time a true computer capable, at a commercial level, of controlling inventories and payrolls, yet which the hobbyist, student and teacher can afford. Programmable for home control applications and for games. The 6502 microprocessor in the upper left is the heart of this miracle chassis.

"We will offer a liquid crystal watch
to retail at \$19.95 . . ."

A liquid crystal display (LCD), completely fabricated in our own plant, is in final test before being placed in a prototype LCD watch.



Commodore's Acquisition of MOS Technology

MOS Technology designs, manufactures and markets large scale integrated circuits, including calculator arrays, microprocessor peripheral devices for microcomputers, 4K bytes and 8K bytes add-on memories for the micro-computer. The company also produces the exciting KIM-1 System, a complete microcomputer on a single card.

MOS is already a supplier to other companies of advanced LSI/MOS four-player game chips for use with either black-and-white or color TV. Not only will this prove profitable to MOS but will also allow your Company to enter the expanding TV game business with a superior product.

The acquisition of MOS will give your Company its first in-house source of MOS circuits for calculators and watches.

Commodore-designed chips will now be produced by MOS and these chips will become part of MOS's expanded production line for sale to the industry.

Commodore accounted for approximately 25% of MOS Technology's volume over the past 3 years. MOS did not produce, however, any of the Commodore-designed chips which comprised 80% of your Company's production.

Commodore's position as a major international company will help MOS to expand its sales world-wide.

As noted in the President's message, the products of MOS, together with those of ODI and our liquid crystal facility will allow us to set up a separate sales division offering components to original equipment manufacturers.

...and the Acquisition of ODI

The acquisition of ODI (Optical Diodes, Inc.), was first announced in the 1975 Annual Report. At the time, ODI was your Company's principal supplier of light-emitting diodes. This marked then the beginning of the vertical integration that has now become a reality.

The acquisition of ODI also contributed to our more rapid entry into the digital watch business; acquired at ODI was a great deal of experience and know-how in what was then a new industry and is even now in its first full growth.

The New Liquid Crystal Facility

The Palo Alto facility is now the location of a new liquid crystal display operation. This pilot manufacturing area is expected to grow to approximately five times its present size by the end of 1977. The operation is already producing field effect liquid crystal watch displays as an internal source for the Company's liquid crystal timepiece programs. Subsequently, we plan to build liquid crystal calculator displays.

———A Partial Line-up of New Products Planned for Introduction this Year.———

A Programmable Calculator — Model PR100 to be introduced in January at considerably under \$100.

Three Dedicated Preprogrammed Calculators — Models N60 (the Navigator), M55 (the Mathematician), and S61 (the Statistician). Specialist calculators with more power than previously available. To retail at \$100. Introduction in January. Test marketing in November.

The Slimmest Rechargeable Calculator — Model X24. Only a half inch thin and to retail before Christmas at \$20 . . . and at least \$10 under market.

The Time Machine — Another first: Performs all basic functions with any units of time (will subtract one date from another, multiply months, hours, etc.). Includes 200 year perpetual calendar and biorhythm plotting. Announcement in January.

Financial Calculators — A series priced from \$19.95 with financial and money-management features. Announcement in January.

Liquid Crystal Display Calculator — Super slim and designed to last over 1000 hours on one set of batteries. Announcement in January.

LED Watch Line — From \$19.95 to \$39.95. European distribution

already begun; North American test marketing in November, full distribution in January.

LCD Watch Line. Basic watch to sell at \$19.95. Announcement in January; distribution in March.

Kim 1 — The first home/hobbyist computer chassis. Distribution already begun by MOS. Retails at under \$250.

NOTE:

Prices where indicated are retails which we expect will prevail in the United States. Prices in Canada, Europe and the Orient may differ somewhat.

Consolidated Statements of Operations

COMMODORE BUSINESS MACHINES (CANADA) LIMITED AND SUBSIDIARIES (NOTE 2)

(Expressed in United States currency)

	Year Ended June 30	
	1976	1975
Net Sales (Note 15)	\$55,934,555	\$55,877,173
Cost of Sales	44,169,912	50,871,487
Gross profit	11,764,643	5,005,686
Operating Expenses:		
Selling	3,490,797	4,071,835
General and administrative	3,366,705	3,941,109
Research and development	812,514	837,492
	7,670,016	8,850,436
Income (loss) from operations	4,094,627	(3,844,750)
Other Income (Expense):		
Interest income on short-term deposits and marketable securities	94,075	111,332
Interest expense	(792,432)	(1,329,317)
	(698,357)	(1,217,985)
Income (loss) before income taxes, minority interest in subsidiaries, and extraordinary item	3,396,270	(5,062,735)
Provision (Credit) For Income Taxes (Notes 5 and 12):		
Current —		
Federal	1,007,000	(1,012,000)
State	116,000	—
Foreign	29,000	78,765
Deferred foreign income taxes	572,000	140,235
	1,724,000	(793,000)
Income (loss) before minority interest in subsidiaries, and extraordinary item	1,672,270	(4,269,735)
Minority Interest in Net Losses of Subsidiaries	49,927	412,730
Income (loss) before extraordinary item	1,722,197	(3,857,005)
Extraordinary Item — Reduction of income taxes from carryforward of prior years' losses	1,189,000	89,000
Net income (loss)	\$ 2,911,197	\$ (3,768,005)
Earnings (Loss) Per Share (United States Method — Note 11):		
Primary —		
Income (loss) before extraordinary item	\$1.34	\$(3.04)
Extraordinary item	.92	.08
Net income (loss)	\$2.26	\$(2.96)
Fully diluted —		
Income (loss) before extraordinary item	\$1.34	\$(3.04)
Extraordinary item	.92	.08
Net income (loss)	\$2.26	\$(2.96)

The accompanying notes to consolidated financial statements are an integral part of these statements.

Consolidated Balance Sheets

COMMODORE BUSINESS MACHINES (CANADA) LIMITED AND SUBSIDIARIES (NOTE 2)

(Expressed in United States Currency)

ASSETS	June 30	
	1976	1975
Current Assets:		
Cash, including short-term deposits of \$734,104 in 1976	\$ 1,159,285	\$ 1,030,811
Deposits pledged as compensating balances for letters of credit	422,665	265,246
Trade receivables, less allowance of \$702,670 in 1976 and \$420,823 in 1975 for doubtful accounts (Notes 4 and 7)	4,042,315	5,550,204
Income taxes recoverable	—	217,895
Advances to suppliers	393,514	266,705
Inventories (Note 7)		
Finished goods	6,203,656	7,141,927
Raw materials and work in process	7,582,447	8,615,142
Total inventory	13,786,103	15,757,069
Prepaid expenses	140,671	144,565
Total current assets	19,944,553	23,232,495
Property and Equipment, at cost (Note 8)	3,976,782	3,041,502
Less — Accumulated depreciation and amortization	1,622,673	1,090,580
	2,354,109	1,950,922
Other Assets:		
Note receivable from Optical Diodes, Inc. (Note 3)	—	375,000
Investments, at cost	13,769	30,835
Lease deposits and other assets	338,094	232,479
Patents, trademarks and other manufacturing rights	1	1
Goodwill, net of accumulated amortization of \$17,000 (Note 3)	183,727	—
	535,591	638,315
	\$22,834,253	\$25,821,732

Approved on behalf of the Board:

Irving Gould, Director

Jack Tramiel, Director

LIABILITIES AND SHAREHOLDERS EQUITY	June 30	
	1976	1975
Current Liabilities:		
Bank overdrafts	\$ 319,820	\$ 151,762
Advances from finance companies, secured by certain receivables and inventories (Note 7)	697,912	1,947,731
Notes payable (Note 6)	2,532,605	2,985,685
Drafts payable	4,654,433	5,750,479
Accounts payable	5,556,262	8,933,614
Accrued liabilities	1,010,348	1,041,607
Obligation under agreement with Optical Diodes, Inc. (Note 3)	—	375,000
Income taxes payable	293,816	211,161
Deferred foreign income taxes	658,621	140,235
Total current liabilities	15,723,817	21,537,274
Long-Term Debt (Note 8)	745,660	732,135
Minority Interest in a Subsidiary	19,000	68,927
Commitments and Contingent Liabilities: (Notes 10 and 13)	—	—
Shareholders' Equity:		
Capital stock (Note 9) —		
Preferred stock, \$10 par value; authorized 100,000 shares, none outstanding	—	—
Common stock, no par value; Authorized — 3,000,000 shares; Outstanding — 1,283,118 shares in 1976 and 1,270,618 shares in 1975	2,057,760	2,016,079
Retained earnings	3,497,078	585,881
Contributed surplus	790,938	881,436
	6,345,776	3,483,396
	\$22,834,253	\$25,821,732

The accompanying notes to consolidated financial statements are an integral part of these consolidated balance sheets.

Consolidated Statements of Changes in Financial Position

COMMODORE BUSINESS MACHINES (CANADA) LIMITED AND SUBSIDIARIES (NOTE 2)

(Expressed in United States currency)

	Year Ended June 30	
	1976	1975
Funds Were Provided By (Used For):		
Operations, exclusive of extraordinary item —		
Income (loss) before extraordinary item, as restated for income tax assessment	\$ 1,722,197	\$ (3,857,005)
Items not requiring outlay of working capital in the current period —		
Depreciation and amortization	739,612	572,740
Write-down of investments	17,066	33,831
Minority interest in loss of a subsidiary	(49,927)	(412,730)
Amortization of goodwill	17,000	—
Total provided by (used for) operations	2,445,948	(3,663,164)
Extraordinary item	1,189,000	89,000
	3,634,948	(3,574,164)
Sale of common stock	41,681	3,600
Increase in long-term debt	13,525	176,020
Decrease in note receivable from Optical Diodes, Inc.	375,000	—
	4,065,154	(3,394,544)
Funds Were Applied To:		
Decrease in long-term debt	—	45,357
Purchase of warrants	90,498	—
Purchase of equipment, building and improvements	1,142,799	799,716
Increase in other assets	105,615	365,858
Acquisition of goodwill associated with Optical Diodes, Inc.	200,727	—
	1,539,639	1,210,931
Increase (decrease) in working capital	\$ 2,525,515	\$ (4,605,475)
Changes in Components of Working Capital:		
Increase (decrease) in current assets —		
Cash	\$ 128,474	\$ 508,241
Deposits pledged	157,419	(317,753)
Receivables and advances to suppliers	(1,381,080)	(2,816,041)
Income taxes recoverable	(217,895)	117,895
Inventories	(1,970,966)	(2,792,816)
Prepaid expenses	(3,894)	(26,772)
(Increase) decrease in current liabilities —		
Advances from finance company	1,249,819	3,106,716
Notes payable, bank overdrafts and ODI obligation	660,022	(159,548)
Accounts and drafts payable and accrued liabilities	4,504,657	(2,804,600)
Income taxes payable	(82,655)	719,438
Deferred foreign income taxes payable	(518,386)	(140,235)
Increase (decrease) in working capital	\$ 2,525,515	\$ (4,605,475)

The accompanying notes to consolidated financial statements are an integral part of these statements.

Consolidated Statements of Shareholders' Equity

COMMODORE BUSINESS MACHINES (CANADA) LIMITED AND SUBSIDIARIES (NOTE 2)

(Expressed in United States Currency)

	Shares	Amount	Retained Earnings	Contributed Surplus	Total
BALANCE, June 30, 1974 as restated (Note 5)	1,269,818	\$2,012,479	\$4,353,886	\$881,436	\$7,247,801
Net loss for the year, as restated (Note 5)	—	—	(3,768,005)	—	(3,768,005)
Sale of common stock upon exercise of warrants	800	3,600	—	—	3,600
BALANCE, June 30, 1975	1,270,618	2,016,079	585,881	881,436	3,483,396
Net income for the year	—	—	2,911,197	—	2,911,197
Sale of common stock upon exercise of options	12,500	41,681	—	—	41,681
Purchase of warrants	—	—	—	(90,498)	(90,498)
BALANCE, June 30, 1976	1,283,118	\$2,057,760	\$3,497,078	\$790,938	\$6,345,776

The accompanying notes to consolidated financial statements are an integral part of these statements.

Notes to Consolidated Financial Statements

1. Summary of Accounting Policies

Principles of Consolidation—The consolidated financial statements include the accounts of Commodore Business Machines (Canada) Limited and all subsidiaries. All such subsidiaries were wholly owned as of June 30, 1976, except for Optical Diodes, Inc. (Note 3), Commodore Educational Systems Limited (Note 4) and Commodore Products Limited which is a 50% owned joint venture created in June, 1976.

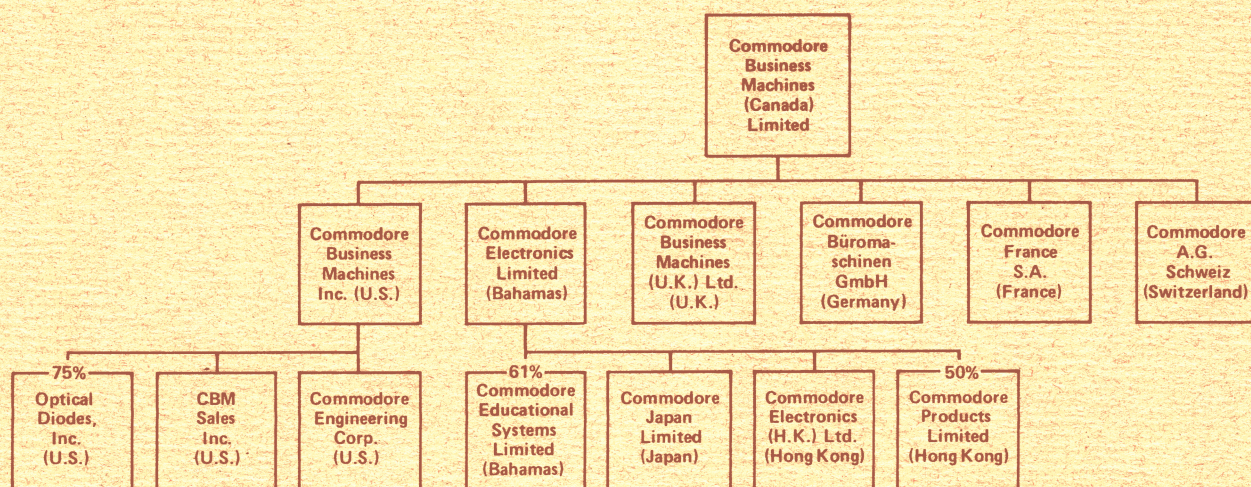
The consolidated financial statements are expressed in United States currency. For foreign operations, monetary assets and liabilities have been translated at year-end rates of exchange and all other assets and liabilities have been translated at historical rates. Income, costs and expenses were translated at average rates prevailing during the year. Gains or losses resulting from translations are included in the consolidated statements of operations. Such gains and losses have not been material.

Inventories—Finished goods and work-in-process inventories include materials, labor and manufacturing overhead. Inventories are stated at the lower of cost (first-in, first-out) or market.

Property and Equipment—

<i>Major classes of property and equipment</i>			
Description	June 30		Estimated Useful Lives
	1976	1975	
Machinery and equipment	\$1,456,095	\$ 881,530	3-10 years
Building and improvements	789,800	781,336	25 years
Furniture and fixtures	377,307	339,356	5-10 years
Tooling	1,138,290	892,750	Expected sales (not to exceed two years)
Leasehold improvements	215,290	146,530	Life of lease
	<u>\$3,976,782</u>	<u>\$3,041,502</u>	

THE COMMODORE GROUP OF COMPANIES PRIOR TO RESTRUCTURING



NOTES:

- 1) All subsidiaries are 100 percent owned, except where indicated.
- 2) Commodore Business Machines (Canada) Limited is a public company, incorporated in the province of Ontario, Canada.
- 3) The country in which each subsidiary is incorporated is indicated.

Notes

Depreciation has been provided using primarily the straight-line method over the estimated useful lives of the assets for both financial reporting and income tax purposes.

Expenditures for maintenance and repairs are charged to expense as incurred. Expenditures for major betterments or renewals are capitalized.

The net gain or loss on items of equipment retired or otherwise disposed of is credited or charged to income and the asset cost and related accumulated depreciation or amortization are removed from the accounts.

Research and Development Costs and Product Development Cost—The company expenses all costs of research and development and product development in the year incurred.

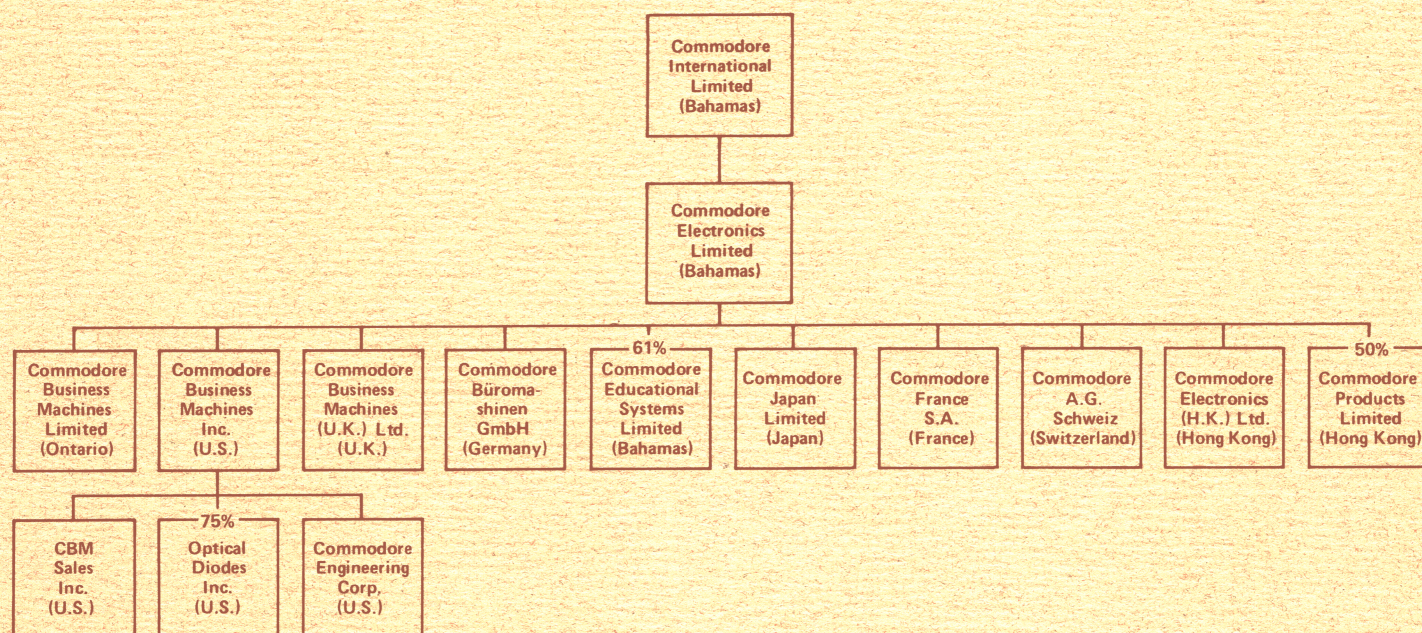
Patents, Trademarks and Other Manufacturing Rights—The company expenses all costs of obtaining patents, trademarks and other manufacturing rights in the year incurred.

Goodwill—Goodwill, which arose in connection with the acquisition of Optical Diodes, Inc. (see Note 3), is amortized on a straight-line basis over a period of four years.

Deferred Income Taxes—Certain transactions or amounts recorded as revenue or expenses in a particular year will enter into the determination of taxable income of different years (timing differences). The most significant of these timing differences relates to special inventory relief provisions in the United Kingdom whereby deductions are allowed for tax reporting purposes prior to recording in the financial statements. Deferred income taxes are provided on these timing differences.

Investment Tax Credits—The company accounts for investment tax credits as a reduction of the provision for taxes on income in the year in which the related credit is utilized. Such credits have not been material. The available investment tax credit carryforward as of June 30, 1976, is not significant.

THE COMMODORE GROUP OF COMPANIES SUBSEQUENT TO RESTRUCTURING



2. Restructuring After End of Fiscal Year

At a general meeting of shareholders on August 17, 1976, the company's proposed plan of restructuring was approved.

This internal restructuring has resulted in each shareholder of the company receiving one share of Commodore International Limited, a Bahamian company, in exchange for each share of the company presently held. Commodore International Limited becomes the parent company of the Commodore group of companies, and the company will surrender its charter under articles of dissolution filed under the Business Corporations Act of Ontario.

The restructuring does not involve transactions which affect the cost basis of assets, or the amount of liabilities shown in the accompanying consolidated financial statements. However, as the shares of Commodore International Limited ultimately held by each shareholder reflect a par value of \$1 U.S. each, the amounts shown in the accom-

panying consolidated balance sheets as capital stock and contributed surplus will, in future years, be reported so as to reflect the pooling of interests method of accounting for the above restructuring.

Shareholders' equity in future consolidated financial statements will be shown as follows for the years 1976 and 1975:

<i>Shareholders' Equity:</i>		
	1976	1975
Capital stock —		
Authorized — 5,000,000 shares, par value \$1 U.S. each		
Issued and outstanding —		
1,283,118 shares in 1976 and 1,270,618 shares in 1975	\$1,283,118	\$1,270,618
Retained earnings	3,497,078	585,881
Contributed surplus	1,565,580	1,626,897
	<u>\$6,345,776</u>	<u>\$3,483,396</u>

Notes

3. Optical Diodes, Inc.

On March 4, 1976, the company acquired a 75% interest in Optical Diodes, Inc. (O.D.I.), a manufacturer of light emitting diodes which are utilized in the company's calculator and watch displays. The company has applied the purchase method of accounting to this transaction and has included the operations of O.D.I. in the accompanying consolidated financial statements for the period since acquisition.

As of March 4, 1976, the company acquired 75% of the outstanding capital stock for a nominal amount. The liabilities exceeded the assets of O.D.I. at the date of acquisition resulting in goodwill on consolidation of \$210,000. This goodwill will be amortized over a period of four years from the date of acquisition in recognition of the potential for technological change existant within the calculator and watch industry.

O.D.I. has experienced losses in prior periods and has losses for tax purposes which may be of future benefit to the company. Any tax benefits which arise from the utilization of tax losses created prior to March 4, 1976, will be applied to the reduction of acquired goodwill.

4. Commodore Educational Systems Limited

The company formed a Bahamian subsidiary, Commodore Educational Systems Limited (CESL) to develop, promote and market, initially in Japan, a table-model language laboratory and teaching machine, together with courses for use in conjunction with this machine. The subsidiary was in the development stage until March 31, 1973.

The sales of CESL are primarily made pursuant to conditional sales contracts and are accounted for on the accrual basis. The unearned interest charged to customers on installment sales is reflected in the accompanying consolidated balance sheets as a reduction from accounts receivable. At June 30, 1976, \$218,325 of accounts receivable are due in installments in the 1977 fiscal year.

CESL has incurred losses of \$3,168,000 since inception.

5. Income Taxes

During 1976, the Internal Revenue Service completed its examination of the 1973 and 1974 federal income tax returns of the company's U.S. subsidiary. This examination resulted in adjustments which, when formally received, will increase income previously reported in 1973 and 1974

federal income tax returns by approximately \$377,000 and \$693,000, respectively. These adjustments do not result in the payment of income taxes as the U.S. subsidiary may carryback its 1975 operating loss in order to offset the adjustments to taxable income. The accompanying financial statements have been retroactively restated to reflect the impact of these adjustments by decreasing the loss in 1975 by \$512,000 (\$.41 per share — U.S. method) and by decreasing retained earnings as of June 30, 1974 by \$512,000.

The Internal Revenue Service is now conducting an examination of the U.S. subsidiary's 1975 income tax return, and management believes that no significant adjustment will result to the previously reported loss for tax purposes.

The credit for federal income taxes of \$1,012,000 in 1975 represents the tax benefit resulting from the carryback of losses incurred by the company's U.S. subsidiary. The 1975 foreign tax provision of \$78,765 includes a credit for Canadian income taxes of \$149,000 representing the tax benefit from the carryback of Canadian operating losses incurred in 1975.

The remaining 1976 and 1975 current and deferred tax provisions have been provided on income of subsidiaries having profitable operations in 1976 and 1975.

6. Notes Payable

<i>Notes payable, June 30</i>		
	1976	1975
15% note payable, secured a collateral mortgage on land owned by companies which are controlled by a director and also by the Chairman of the Board, due April, 1976	\$ —	\$1,000,000
10% note payable to Diversified Credit Corporation (a Bahamian corporation owned by the Company's Chairman of the Board), unsecured, due on demand	—	17,500
Notes payable to banks	2,436,925	1,879,181
12% note payable, unsecured, due on demand	50,000	50,000
Current portion of long-term debt	45,680	39,004
	<u>\$2,532,605</u>	<u>\$2,985,685</u>

Approximately \$1,660,463 of the notes payable to banks at June 30, 1976, are unsecured. The notes involve one bank as of June 30, 1976, with balances ranging from \$200,000 to \$545,945. The notes are generally due on demand and bear interest at rates ranging from 6½% to 12½% per annum.

During fiscal 1976, the highest balance owing to banks was \$2,544,000 (1975—\$2,250,000), the average balance owing to banks was \$1,994,000 (1975—\$2,030,000), and the weighted average interest rate was 9½% (1975—13%).

7. Advances from Finance Companies

The company has agreements with two finance companies whereby the company may pledge certain receivables and inventories and other assets, with interest ranging from 1½% to 6½% over the prime rate in effect, depending on the amount borrowed. During the fiscal year ending June 30, 1976, the highest balance owing was \$904,000 (1975—\$5,319,000), the average balance owing was \$740,000 (1975—\$3,918,000), with a weighted average interest rate during the year of 16% (1975—14½%). As of June 30, 1976, trade receivables of approximately \$872,000 (1975—\$3,345,000), and other assets, primarily inventories, of approximately \$980,000 (1975—\$7,052,000), were pledged as security for advances from the two finance companies.

8. Long-Term Debt

Long Term Debt Obligations, June 30

	1976	1975
Mortgage note payable	\$592,823	\$601,472
Contracts payable	198,517	169,667
	791,340	771,139
Less—Current portion (see Note 6)	45,680	39,004
	<u>\$745,660</u>	<u>\$732,135</u>

Mortgage Note Payable—During fiscal 1974, the company borrowed \$615,000 to finance the acquisition of a building and improvements. The mortgage note balance at June 30, 1976, of \$592,823, is repayable over 23 years with interest at 8½%. The loan is secured by a deed of trust on the building.

Contracts Payable—The company acquired certain equipment under installment contracts totaling approximately \$198,517 payable monthly over periods of from 3 to 7 years, with interest averaging 11%.

9. Stock Options and Share Purchase Warrants

As of June 30, 1976, the company has reserved 150,000 shares of common stock for exercise of stock options. No shares of common stock were reserved for share purchase warrants.

Employee Stock Option Plan—The company has reserved 62,000 shares of common stock for issuance to key employees under the company's Employee Stock Option Plan. The company's plan, instituted in 1974, was designed to qualify under Section 422 of the U.S. Internal Revenue Code, as amended, under the terms of which the company and its subsidiaries may grant options to certain key employees to purchase up to 150,000 shares of the company's common stock. The plan is administered by the Board of Directors of the company. The option price may not be less than 100% of the fair market value of the shares at the date of grant. Options granted are exercisable in cumulative annual increments of 33% after the first nine months after the date of grant and expire five years from date of grant. Cancelled options become available for future grant.

Prior to 1974, the company did have another option plan. However, the last of the share options, exercisable under the former option plan, were exercised in May, 1976.

The following table summarizes options outstanding at June 30, 1976, and the number of options exercised under the plans during the two years ended June 30, 1976 (amounts are in Canadian dollars).

Options Outstanding June 30, 1976

	Number of Shares	Option Price	
		Per Share	Total
Options outstanding at June 30, 1976 were granted during (new plan only)—			
1974	10,000	\$6.69	\$ 66,900
1975	14,000	\$2.25 to \$4.33	39,800
1976	38,000	\$3.25	123,500
Total	<u>62,000</u>		<u>\$230,200</u>
Options exercised during—			
1975	—	—	—
1976 (old plan)	<u>12,500</u>	<u>\$3.25</u>	<u>\$ 40,625</u>

Notes

There were 13,667 shares exercisable under the company's new plan at June 30, 1976.

There were 88,000 shares as of June 30, 1976, and 111,000 shares as of June 30, 1975, available for grant.

The proceeds from the exercise of stock options are credited to the common stock account. No charges or credits are made to income in connection with stock option transactions.

Share Purchase Warrants—At June 30, 1975, the company had reserved 94,500 shares of common stock for exercise of the outstanding Series "C" Share Purchase Warrants issued in prior years. The Share Purchase Warrants entitled the holders thereof to purchase an equal number of fully-paid, non-assessable shares of common stock at a price of \$5.50 on or before April 1, 1976. 194,175 Series "A" and 51,000 Series "B" Share Purchase Warrants expired during fiscal 1975.

In March, 1976, the company repurchased 88,550 of the Series "C" warrants at the cost of CDN \$1.00 per warrant. The cost of these repurchased warrants was charged to Contributed Surplus.

10. Commitments and Contingent Liabilities

In June, 1976, the company concluded an agreement with Komy Corporation, whose affiliate is an assembler of MOS integrated circuits, LED displays and watch modules for the company. The agreement includes an assembly contract amounting to approximately \$4,200,000, which will run until August 31, 1978, or until all of the product has been supplied. The agreement also includes a provision whereby the company can exercise an option to acquire the fixed assets of the assembly company for \$1,131,000.

At June 30, 1976, some of the premises utilized by the company and its subsidiaries were occupied under long-term leases which expire at various dates to 1992. Annual rentals were \$328,000 in 1976, and \$288,000 in 1975. Aggregate minimum rental commitments remaining under these lease contracts after June 30, 1976, are as follows:

<i>Rental Commitments</i>	
Fiscal Year Ending June 30	Amount
1977	\$157,000
1978	113,000
1979	104,000
1980	86,000
1981	81,000
1982-1986	238,000
1987-1991	44,000
Total remaining obligations as of June 30, 1976	<u>\$823,000</u>

The company also has a purchase option to acquire land and buildings located in England for \$450,000. The company currently has a lease on this property which will expire on April 30, 1977. The option is exercisable not less than 90 days before the expiration date of the lease.

As of June 30, 1976, the company has purchase commitments of approximately \$3,860,000, which are cancellable under certain conditions, for future delivery of parts.

The company is contingently liable at June 30, 1976, for trade receivables of approximately \$1,140,000, which have been discounted at banks. Additionally, the company is contingently liable for approximately \$579,000 of notes receivable given by customers to financial institutions.

11. Earnings Per Share

United States Method

Earnings per share have been computed by dividing net income (loss) by the weighted average number of common shares and common share equivalents outstanding during each period (except that common share equivalents were excluded in 1975 because the effect would be anti-dilutive).

Common shares and common share equivalents included in these computations are summarized in the following tabulations.

<i>Common Shares and Equivalents— U.S. Method</i>		
	1976	1975
Weighted Average Common Shares Outstanding During the Years	1,272,701	1,270,435
Effect of Assumed Exercise of Dilutive Stock Options and Warrants	15,430	—
Total Common Shares and Common Share Equivalents	1,288,131	1,270,435
Common Shares, Assuming Full Dilution*	1,288,131	1,270,435
*Additional common shares from exercise of dilutive stock options and warrants result from the use of the market price of common stock at the end of the year rather than the average price during the year in applying the treasury stock method. In 1975, the effect of including stock options and warrants in the computation of fully-diluted earnings per share would be anti-dilutive and, accordingly, such effect is not shown.		

Canadian Method

Basic earnings per share are based upon the weighted average number of shares outstanding during each year. Fully diluted earnings per share have been calculated by assum-

ing that the proceeds from the exercise of stock options and warrants have been applied to reflect a reduction in the borrowing costs incurred by the company. This results in an increase in net income of approximately \$38,000 in 1976 for purposes of this calculation.

<i>Earnings Per Share—restated, Canadian Method</i>		
	1976	1975
Basic		
Income (Loss) Before Extraordinary Item	\$1.35	\$(3.04)
Net Income (Loss)	2.29	(2.97)
Fully Diluted		
Income (Loss) Before Extraordinary Item	1.25	(3.04)
Net Income (Loss)	2.09	(2.97)

In 1975, the effect of including stock options and warrants in the computation of fully-diluted earnings per share would have been anti-dilutive.

<i>Common Shares and Equivalents—Canadian Method</i>		
	1976	1975
Weighted Average Common Shares Outstanding During the Year	1,272,701	1,270,435
Effect of Assumed Exercise of Stock Options and Warrants	134,958	—
Total Common Shares, Assuming Full Dilution	1,407,659	1,270,435

12. Results of Operations—Fiscal 1976

Because of uncertainties with respect to the outcome of an Internal Revenue Service (IRS) examination in process at June 30, 1975, and with respect to the realization of inventories and property and equipment, the auditors' report on the 1975 consolidated financial statements was qualified.

The IRS examination has since been completed and as a result, the consolidated financial statements have been retroactively restated for 1975 to give recognition to the income tax assessments to be received (see Note 5).

Also, the electronic calculator industry stabilized during the company's 1976 fiscal year and the company returned to profitable operations and substantially improved its working capital position.

Thus, the uncertainties that caused the auditors to qualify their opinion on the 1975 consolidated financial statements have been removed.

13. Litigation

A number of legal actions have been brought against the company and/or its subsidiaries primarily by certain suppliers. The actions brought by the suppliers generally allege breach of contract relating to component parts for assembly of calculators which the company has found to be defective or not suitable, and has either returned to the supplier or withheld payment, or both. During the year ended June 30, 1976, the company settled the most important of the cases against it without any significant loss. Based upon the opinions of counsel, management believes that the ultimate settlement of all currently pending legal actions will not have a material effect upon the company's financial position or results of operations.

14. Foreign Operations

The sales, assets and current liabilities of the company's foreign operations (outside North America)

	(Dollars in thousands)	
	1976	1975
Sales	\$43,100	\$32,560
Assets		
Current	13,339	12,600
Other	907	700
Current Liabilities	10,179	10,700

15. Operations—Related Parties

Sales include approximately \$1,000,000 in 1976 and 1975 to companies which are owned or effectively controlled by the Chairman of the company's Board of Directors. Included in accounts receivable as of June 30, 1976 and 1975, was approximately \$154,000 and \$14,000, respectively, representing amounts owing from these companies.

The company currently is managing the operations of Gildon Metal Enterprises Limited and Nortex Products, respectively a subsidiary and a division of Superpack Corporation Limited. The terms of this arrangement have not been formalized, though the company expects to continue to manage the above operation in the 1977 fiscal year. The Chairman of the company's Board of Directors is also the Chairman of the Board of Superpack Corporation Limited.

The company's Japanese subsidiary, Commodore Japan Limited (CJL), utilizes a Japanese company for the assembly of products and another Japanese company for certain research and development activities relating to electronic calculators. Both of these companies are controlled by the President of CJL. Virtually all of the production of the assembly company is for CJL. In 1976 assembly charges

Notes

and related services paid by CJL to the assembly company approximated \$1,397,000. Charges paid by CJL to the research and development company approximated \$221,000 in 1976 and the relationship was terminated on June 30, 1976. At June 30, 1976, CJL had receivables from and advances to these companies aggregating \$257,000 and accounts and notes payable to these companies of \$508,000.

16. Remuneration of Directors and Senior Officers

Aggregate direct remuneration paid or payable by the company and its subsidiaries for 1976 to directors and senior officers of the parent company was approximately \$317,000 (1975-\$285,000).

17. Subsequent Event

The company is currently negotiating to acquire ownership of MOS Technology, Inc. (MOS Tech), a Delaware

corporation, which manufactures and sells integrated circuits based upon metal-oxide-semiconductor (MOS) technology. In this connection, the company has made the following commitments:

- a. The company has guaranteed a \$700,000 line of accounts receivable financing to MOS Tech by Berkeley Service Corporation, an affiliate of The Chase Manhattan Bank, N.A.
- b. The company has loaned \$500,000 to MOS Tech.

Both of these commitments are secured by the company having a lien on the assets of MOS Tech and also on 80% of the voting stock of MOS Tech.

At February 29, 1976, the date of the most recent audited statements, the net assets of MOS Tech amounted to \$949,000; the net sales for the thirteen months ended February 29, 1976, were \$11,368,000; and the net loss was \$16,000.

Auditors' Report

To the Shareholders of Commodore Business Machines (Canada) Limited:

We have examined the consolidated balance sheets of Commodore Business Machines (Canada) Limited (an Ontario corporation) and subsidiaries as of June 30, 1976 and 1975, and the related consolidated statements of operations, shareholders' equity and changes in financial position for the years then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the financial statements referred to above present fairly the financial position of Commodore Business Machines (Canada) Limited and subsidiaries as of June 30, 1976 and 1975, and the results of their operations and the changes in their financial position for the years then ended, in conformity with generally accepted accounting principles consistently applied during the periods.

ARTHUR ANDERSEN & CO.
Chartered Accountants

Toronto, Canada,
September 28, 1976

BOARD OF DIRECTORS

Irving Gould
Chairman of the Board of
Directors of the Company
Coral Harbour, N.P., Bahamas

Jack Tramiel
President of the Company
Saratoga, California

Burton Winberg
Toronto, Ontario

Vincent Peter Paul
Toronto, Ontario

Gerald Shefsky
Toronto, Ontario

OFFICERS

Irving Gould
Chairman of the Board

Jack Tramiel
President

Christopher T. G. Fish
Vice-President and Secretary

Gerald van Buskirk
Vice-President

Samuel Bernstein
Vice-President

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The Canadian Bank of
Commerce Trust Company
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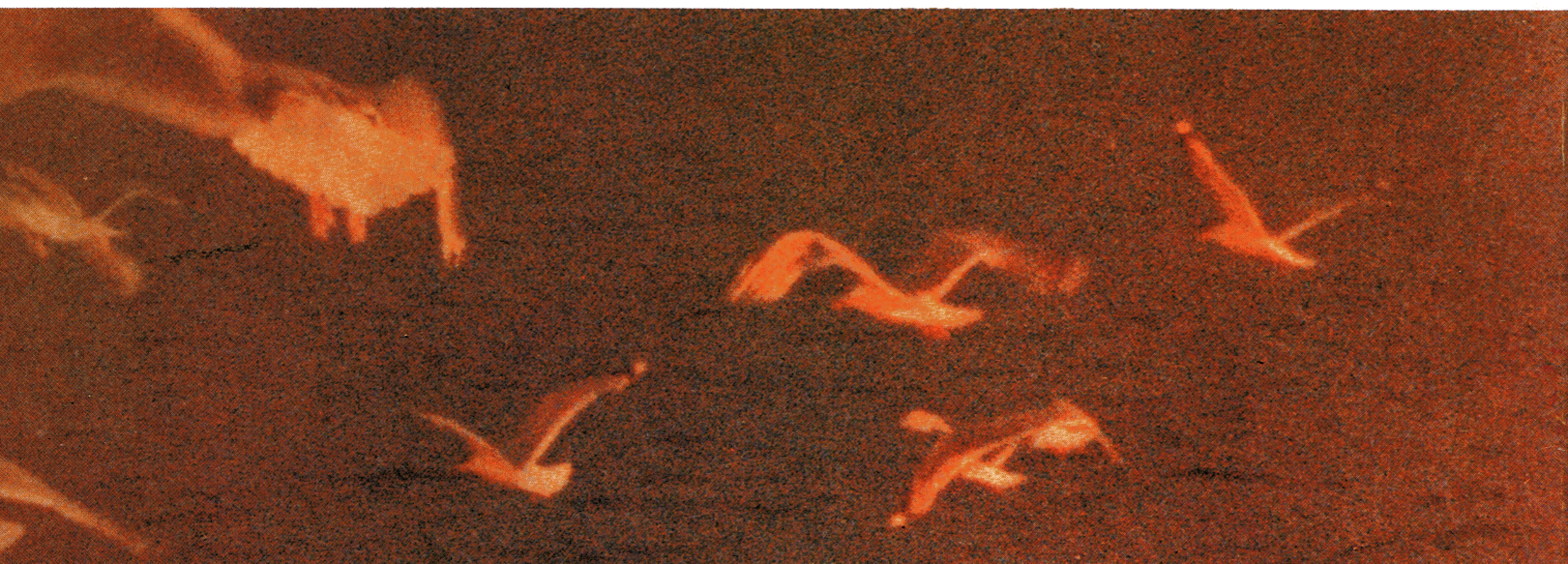
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